

FLEXIBLE SOLUTIONS INTERNATIONAL INC
Form 10-Q
May 14, 2010

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, DC 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2010

OR

TRANSITION REPORT PURSUANT TO 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 001-31540

FLEXIBLE SOLUTIONS INTERNATIONAL INC.

(Exact Name of Issuer as Specified in Its Charter)

Nevada

91-1922863

(State or other jurisdiction of incorporation
or organization)

(I.R.S. Employer Identification No.)

615 Discovery St.
Victoria, British Columbia, Canada

V8T 5G4

(Address of Issuer's Principal Executive Offices)

(Zip Code)

Issuer's telephone number: (250) 477-9969

N/A

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) had been subject to such filing requirements for the past 90 days.

Yes

No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check One):

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Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the Registrant is a shell company (as defined in Exchange Act Rule 12b-2 of the Exchange Act).

Yes

No

<u>Class of Stock</u>	<u>No. Shares Outstanding</u>	<u>Date</u>
Common	13,962,567	April 30, 2010

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This document contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact are “forward-looking statements” for the purposes of the federal and state securities laws, including, but not limited to: any projections of earnings, revenue or other financials items; any statements of the plans, strategies and objectives of management for future operations; any statements concerning proposed new services or developments; any statements regarding future economic conditions or performance; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing.

Forward-looking statements may include the words “may,” “could,” “will,” “estimate,” “intend,” “continue,” “believe,” “expect” or “anticipate” or other similar words. These forward-looking statements present our estimates and assumptions only as of the date of this report. Except for our ongoing obligation to disclose material information as required by the federal securities laws, we do not intend, and undertake no obligation, to update any forward-looking statement.

Although we believe that the expectations reflected in any of our forward-looking statements are reasonable, actual results could differ materially from those projected or assumed in any of our forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to change and inherent risks and uncertainties. The factors impacting these risks and uncertainties include but are not limited to:

- Increased competitive pressures from existing competitors and new entrants;
- Increases in interest rate or our cost of borrowing or a default under any material debt agreement;
- Deterioration in general or regional economic conditions;
- Adverse state or federal legislation or regulation that increases the costs of compliance, or adverse findings by a regulator with respect to existing operations;
- Loss of customers or sales weakness;
- Inability to achieve future sales levels or other operating results;
- The unavailability of funds for capital expenditures; and
- Operational inefficiencies in distribution or other systems.

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For a detailed description of these and other factors that could cause actual results to differ materially from those expressed in any forward-looking statement, please see "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2009.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

FLEXIBLE SOLUTIONS INTERNATIONAL, INC.

CONSOLIDATED BALANCE SHEETS

At March 31, 2010

(U.S. Dollars)

	March 31, 2010 (Unaudited)	December 31, 2009
Assets		
Current		
Cash and cash equivalents	\$ 1,635,930	\$ 2,126,150
Accounts receivable	2,112,830	1,544,364
Inventory	2,998,962	2,796,307
Prepaid expenses	119,193	121,353
	6,866,915	6,588,175
Property, equipment and leaseholds		
	7,472,227	7,314,926
Patents	229,241	224,505
Long term deposits	7,741	7,499
Deferred tax asset	119,000	119,000
	\$ 14,695,124	\$ 14,254,105
Liabilities		
Current		
Accounts payable and accrued liabilities	\$ 455,549	\$ 597,307
Taxes payable	129,000	304,000
Current portion of long term debt	106,420	74,146
	690,969	975,453
Long Term		
Loans	2,257,913	2,211,168
	\$ 2,948,882	\$ 3,186,621
Stockholders' Equity		
Capital stock		
Authorized		
50,000,000 Common shares with a par value of \$0.001 each		
1,000,000 Preferred shares with a par value of \$0.01 each		
Issued and outstanding		
13,962,567 (2009: 13,962,567) common shares	13,963	13,963
Capital in excess of par value	16,485,088	16,456,903
Other comprehensive income	466,109	331,208
Deficit	(5,218,918)	(5,734,591)
Total Stockholders' Equity	11,746,242	11,067,483

Total Liabilities and Stockholders' Equity	\$ 14,695,124	\$ 14,254,105
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Commitments, Contingencies and Subsequent Events (Notes 13, 14 & 15)

-- See Notes to Unaudited Consolidated Financial Statements --

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FLEXIBLE SOLUTIONS INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

For the Three Months Ended March 31, 2010 and 2009

(U.S. Dollars -- Unaudited)

	Three Months Ended March 31,	
	2010	2009
Sales	\$ 3,384,846	\$ 2,659,548
Cost of sales	1,852,532	2,012,546
Gross profit	1,532,314	647,002
Operating expenses		
Wages	377,153	306,590
Administrative salaries and benefits	84,355	88,431
Advertising and promotion	28,774	22,072
Investor relations and transfer agent fee	23,496	38,256
Office and miscellaneous	100,206	56,698
Insurance	50,616	52,903
Interest expense	18,742	11,385
Rent	41,183	56,619
Consulting	33,227	27,475
Professional fees	41,611	42,488
Travel	25,503	31,212
Telecommunications	9,772	6,783
Shipping	5,868	10,385
Research	18,855	2,894
Commissions	42,384	23,705
Bad debt expense (recovery)	5,253	(590)
Currency exchange	10,284	(13,518)
Utilities	30,359	13,443
Total operating expenses	947,641	780,231
Operating Income (loss)	584,673	(133,229)
Interest income	—	78
Income (loss) before income tax	584,673	(133,151)
Provision for income taxes	(69,000)	—
Net income (loss)	515,673	(133,151)
Net income (loss) per share (basic and diluted)	\$ 0.04	\$ (0.01)
Weighted average number of common shares	13,962,567	14,062,567

FLEXIBLE SOLUTIONS INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Three Months Ended March 31, 2010 and 2009

(U.S. Dollars -- Unaudited)

	Three Months Ended March 31,	
	2010	2009
Operating activities		
Net income (loss)	\$ 515,673	\$ (133,229)
Stock compensation expense	28,186	66,292
Depreciation	86,738	100,083
Changes in non-cash working capital items:		
(Increase) Decrease in accounts receivable	(565,878)	(468,668)
(Increase) Decrease in inventory	(180,130)	299,484
(Increase) Decrease in prepaid expenses	3,630	46,621
Increase (Decrease) in accounts payable	(40,167)	(40,167)
Increase (Decrease) in taxes payable	69,000	—
Cash provided by (used in) operating activities	(429,588)	(129,584)
Investing activities		
Long term deposits	—	5,606
Development of patents	—	9,783
Acquisition of property and equipment	(76,320)	(205,760)
Cash provided by (used in) investing activities	(76,320)	(190,371)
Financing activities		
Loan	—	(61,092)
Proceeds from issuance of common stock	—	—
Cash provided by financing activities	—	(61,092)
Effect of exchange rate changes on cash	15,688	(4,741)
Inflow (outflow) of cash	(490,220)	(385,788)
Cash and cash equivalents, beginning	2,126,150	1,894,045
Cash and cash equivalents, ending	\$ 1,635,930	\$ 1,508,257
Supplemental disclosure of cash flow information:		
Income taxes paid	\$ 69,000	—
Interest paid	\$ 18,742	\$ 11,385

-- See Notes to Unaudited Consolidated Financial Statements --

FLEXIBLE SOLUTIONS INTERNATIONAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the Period Ended March 31, 2010

(U.S. Dollars)

1. BASIS OF PRESENTATION.

These unaudited consolidated financial statements of Flexible Solutions International, Inc (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information. These financial statements are condensed and do not include all disclosures required for annual financial statements. The organization and business of the Company, accounting policies followed by the Company and other information are contained in the notes to the Company's audited consolidated financial statements filed as part of the Company's December 31, 2009 Annual Report on Form 10-K. This quarterly report should be read in conjunction with such annual report.

In the opinion of the Company's management, these consolidated financial statements reflect all adjustments necessary to present fairly the Company's consolidated financial position at March 31, 2010, and the consolidated results of operations and the consolidated statements of cash flows for the three months ended March 31, 2010 and 2009. The results of operations for the three months ended March 31, 2010 are not necessarily indicative of the results to be expected for the entire fiscal year.

These consolidated financial statements include the accounts of Flexible Solutions International, Inc. (the "Company"), and its wholly-owned subsidiaries Flexible Solutions, Ltd. ("Flexible Ltd.") and NanoChem Solutions Inc. All inter-company balances and transactions have been eliminated. The Company was incorporated May 12, 1998 in the State of Nevada and had no operations until June 30, 1998.

The Company and its subsidiaries develop, manufacture and market specialty chemicals which slow the evaporation of water. The Company's primary product, HEAT\$AVR®, is marketed for use in swimming pools and spas where its use, by slowing the evaporation of water, allows the water to retain a higher temperature for a longer period of time and thereby reduces the energy required to maintain the desired temperature of the water in the pool. Another product, WATER\$AVR®, is marketed for water conservation in irrigation canals, aquaculture, and reservoirs where its use slows water loss due to evaporation. In addition to the water conservation products, the Company also manufactures and markets water-soluble chemicals utilizing thermal polyaspartate biopolymers (hereinafter referred to as "TPAs"), which are beta-proteins manufactured from the common biological amino acid, L-aspartic. TPAs can be formulated to prevent corrosion and scaling in water piping within the petroleum, chemical, utility and mining industries. TPAs are also used as proteins to enhance fertilizers in improving crop yields and as additives for household laundry detergents, consumer care products and pesticides.

2. SIGNIFICANT ACCOUNTING POLICIES.

These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States applicable to a going concern and reflect the policies outlined below.

- (a) *Cash and Cash Equivalents.*

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The Company considers all highly liquid investments purchased with an original or remaining maturity of less than three months at the date of purchase to be cash equivalents. Cash and cash equivalents are maintained with several financial institutions.

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(b) *Inventories and Cost of Sales*

The Company has four major classes of inventory: finished goods, work in progress, raw materials and supplies. In all classes, inventory is valued at the lower of cost and market. Cost is determined on a first-in, first-out basis. Cost of sales includes all expenditures incurred in bringing the goods to the point of sale. Inventory costs and costs of sales include direct costs of the raw material, inbound freight charges, warehousing costs, handling costs (receiving and purchasing) and utilities and overhead expenses related to the Company's manufacturing and processing facilities.

(c) *Allowance for Doubtful Accounts*

The Company provides an allowance for doubtful accounts when management estimates collectibility to uncertain. Accounts receivable are continually reviewed to determine which, if any, accounts are doubtful of collection. In making the determination of the appropriate allowance amount, the Company considers current economic and industry conditions, relationships with each significant customer, overall customer credit-worthiness and historical experience.

(d) *Property, Equipment and Leaseholds.*

The following assets are recorded at cost and depreciated using the methods and annual rates shown below:

Computer hardware	30% Declining balance
Automobile	30% Declining balance
Trade show booth	30% Declining balance
Furniture and fixtures	20% Declining balance
Manufacturing equipment	20% Declining balance
Office equipment	20% Declining balance
Building and improvements	10% Declining balance
Leasehold improvements	Straight-line over lease term

Depreciation is recorded at half for the year the assets are first purchased. Property and equipment are written down to net realizable value when management determines there has been a change in circumstances which indicates its carrying amount may not be recoverable. No write-downs have been necessary to date.

Costs capitalized on self-constructed assets classified as plant under construction, include contracted costs and supplies, but do not capitalize interest costs. The Company does not commence depreciating its plant under construction until it becomes operational.

(e) *Impairment of Long-Lived Assets.*

In accordance with FASB Codification Topic 360, "Property, Plant and Equipment (ASC 360), the Company reviews long-lived assets, including, but not limited to, property and equipment, patents and other assets, for impairment annually or whenever events or changes in circumstances

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indicate the carrying amounts of assets may not be recoverable. The carrying value of long-lived assets is assessed for impairment by evaluating operating performance and future undiscounted cash flows of the underlying assets. If the sum of the expected future cash flows of an asset is less than its carrying value, an impairment measurement is indicated. Impairment charges are recorded to the extent that an asset's carrying value exceeds its fair value. Accordingly, actual results could vary significantly from such estimates. There were no impairment charges during the periods presented.

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(f) *Foreign Currency.*

The functional currency of one of the Company's subsidiaries is the Canadian Dollar. The translation of the Canadian Dollar to the reporting currency of the U.S. Dollar is performed for assets and liabilities using exchange rates in effect at the balance sheet date. Revenue and expense transactions are translated using average exchange rates prevailing during the year. Translation adjustments arising on conversion of the financial statements from the subsidiary's functional currency, Canadian Dollars, into the reporting currency, U.S. Dollars, are excluded from the determination of income (loss) and are disclosed as other comprehensive income (loss) in stockholders' equity.

Foreign exchange gains and losses relating to transactions not denominated in the applicable local currency are included in operating income (loss) if realized during the year and in comprehensive income (loss) if they remain unrealized at the end of the year.

(g) *Revenue Recognition.*

Revenue from product sales is recognized at the time the product is shipped since title and risk of loss are transferred to the purchaser upon delivery to the carrier. Shipments are made F.O.B. shipping point. The Company recognizes revenue when there is persuasive evidence of an arrangement, delivery to the carrier has occurred, the fee is fixed or determinable, collectibility is reasonably assured and there are no significant remaining performance obligations. When significant post-delivery obligations exist, revenue is deferred until such obligations are fulfilled. To date there have been no such significant post-delivery obligations.

Provisions are made at the time the related revenue is recognized for estimated product returns. Since the Company's inception, product returns have been insignificant; therefore no provision has been established for estimated product returns.

(h) *Stock Issued in Exchange for Services.*

The Company's common stock issued in exchange for services is valued at an estimated fair market value based upon trading prices of the Company's common stock on the dates of the stock transactions. The corresponding expense of the services rendered is recognized over the period that the services are performed.

(i) *Stock-based Compensation.*

The Company recognizes compensation expense for all share-based payments, in accordance with FASB Codification Topic 718, *Compensation — Stock Compensation*, (ASC 718). Under the fair value recognition provisions of ASC 718, the Company recognizes share-based compensation expense, net of an estimated forfeiture rate, over the requisite service period of the award.

Shares of newly issued common stock will be issued upon exercise of stock options or vesting of restricted share units.

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The fair value at grant date of stock options is estimated using the Black-Scholes-Merton option-pricing model. Compensation expense is recognized on a straight-line basis over the stock option vesting period based on the estimated number of stock options that are expected to vest.

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(j) *Comprehensive Income.*

Other comprehensive income refers to revenues, expenses, gains and losses that under generally accepted accounting principles are included in comprehensive income, but are excluded from net income as these amounts are recorded directly as an adjustment to stockholders' equity. The Company's other comprehensive income is primarily comprised of unrealized foreign exchange gains and losses.

(k) *Income (loss) Per Share.*

Basic earnings (loss) per share is computed by dividing income (loss) available to common stockholders by the weighted average number of common shares outstanding in the period. Diluted earnings (loss) per share are calculated giving effect to the potential dilution of the exercise of options and warrants.

(l) *Use of Estimates.*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and would impact the results of operations and cash flows.

(m) *Financial Instruments.*

The fair market value of the Company's financial instruments comprising cash and cash equivalents, accounts receivable, long term deposits and accounts payable were estimated to approximate their carrying values due to immediate or short-term maturity of these financial instruments. The Company maintains cash balances at financial institutions which at times, exceed federally insured amounts. The Company has not experienced any material losses in such accounts.

The Company is exposed to foreign exchange and interest rate risk to the extent that market value rate fluctuations materially differ from financial assets and liabilities, subject to fixed long-term rates.

(n) *Fair Value of Financial Instruments*

In August 2009, an update was made to *Fair Value Measurements and Disclosures* — "*Measuring Liabilities at Fair Value.*" This update permits entities to measure the fair value of liabilities, in circumstances in which a quoted price in an active market for an identical liability is not available, using a valuation technique that uses a quoted price of an identical liability when traded as an asset, quoted prices for similar liabilities or similar liabilities when traded as assets or the income or market approach that is consistent with the principles of *Fair Value Measurements and Disclosures*. Effective upon issuance, the Company has adopted this guidance with no material impact to the Company's consolidated financial statements.

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Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs described below, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

- Level 1 – Quoted prices in active markets for identical assets or liabilities

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- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The fair values of cash and cash equivalents, accounts receivable, long term deposits and accounts payable for all periods presented approximate their respective carrying amounts due to the short term nature of these financial instruments. The fair values of long term debt approximate their carrying amounts as they bear market rates of interest.

(o) *Contingencies*

Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to the Company but which will only be resolved when one or more future events occur or fail to occur. The Company's management and its legal counsel assess such contingent liabilities, and such assessment inherently involves an exercise of judgment. In assessing loss contingencies related to legal proceedings that are pending against the Company or unasserted claims that may result in such proceedings, the Company's legal counsel evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein.

If the assessment of a contingency indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, the estimated liability would be accrued in the Company's financial statements. If the assessment indicates that a potential material loss contingency is not probable but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, would be disclosed.

Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the guarantees would be disclosed.

(p) *Income Taxes*

Federal, state and foreign income taxes are computed at current tax rates, less tax credits. Provisions for income taxes include amounts that are currently payable, plus changes in deferred income tax assets and liabilities. Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the expected future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred tax assets are reduced by a valuation allowance so that the assets are recognized only to the extent that when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will be realized.

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(q) *Risk Management*

The Company's credit risk is primarily attributable to its accounts receivable. The amounts presented in the accompanying consolidated balance sheets are net of allowances for doubtful accounts, estimated by the Company's management based on prior experience and the current economic environment. The Company is exposed to credit-related losses in the event of non-performance by counterparties to the financial instruments. Credit exposure is minimized by dealing with only credit worthy counterparties. Accounts receivable for the three primary customers totals \$1,029,999 (49%) as at March 31, 2010 (2009 - \$1,030,960 or 67%).

The credit risk on cash and cash equivalents is limited because the Company limits its exposure to credit loss by placing its cash and cash equivalents with major financial institutions.

The Company is not exposed to significant interest rate risk to the extent that long term debt owed to foreign government agencies is subject to a fixed rate of interest.

In order to manage its exposure to foreign exchange risks, the Company is closely monitoring the fluctuations in the foreign currency exchange rates and the impact on the value of cash and cash equivalents, accounts receivable, and accounts payable.

(r) *Recent Accounting Pronouncements*

In October 2009, the FASB issued Accounting Standards Update (ASU) 2009-13, *Multiple-Deliverable Revenue Arrangement* (ASU 2009-13), which amends Codification Topic 605, *Revenue Recognition*. This update provides amendments to the criteria for separating deliverables, measuring and allocating arrangement consideration to one or more units of accounting. This update also establishes a selling price hierarchy for determining the selling price of a deliverable. ASU 2009-13 is effective for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The Company is currently evaluating the impact the adoption of the update may have on its consolidated results of operations and financial position.

In June 2009, the FASB issued ASU No. 2009-1 to FASB Codification Topic 105, *Generally Accepted Accounting Principles*, based on SFAS No. 168, *FASB Accounting Guidance Standards Codification and the Hierarchy of Generally Accepted Accounting Principles — a replacement of SFAS No. 162*. This statement establishes that the FASB Codification becomes the single official source of authoritative U.S. GAAP superseding all non-SEC accounting and reporting standards and literature. Only one level of authoritative U.S. GAAP will exist and all other literature will be considered non-authoritative. The FASB Codification became effective for interim and annual periods ending on or after September 15, 2009. The Company adopted the FASB Codification beginning in the fourth quarter of fiscal 2009. Given that the FASB Codification does not change U.S. GAAP, this statement had no impact on the Company's consolidated financial condition or results of operations. Where possible, previously disclosed FASB references have been replaced with FASB Codification references.

In June 2009, an update was made to ASC 810, *Consolidation*. This update amends previous guidance to require the Company to perform an analysis to determine whether its variable interests give it a controlling financial interest in a variable interest entity. The update is effective for annual periods beginning after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. The Company is currently evaluating the impact the adoption of the update may have on its consolidated results of operations and financial position.

In May 2009, the FASB issued guidance which is included in FASB Codification Topic 855, *Subsequent Events*, (ASC 855). ASC 855 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. The Company

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has evaluated subsequent events through March 31, 2010 for appropriate accounting and disclosure in accordance with this standard.

In April 2009, the FASB issued guidance which is included in FASB Codification Topic 320, *Investments — Debt and Equity Securities*, (ASC 320). ASC 320 amended the other-than-temporary impairment guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities. The Company's implementation of this standard on May 1, 2009 did not have a significant impact on its consolidated statements of operations and financial position.

3. Accounts Receivable

	2010	2009
Accounts receivable	\$ 2,126,856	\$ 1,552,723
Allowances for doubtful accounts	(14,026)	(8,359)
	\$ 2,112,830	\$ 1,544,364

The Company has pledged \$350,748 of the above listed accounts receivable as collateral for the Flexible Solutions Ltd. loan from AFSC (see Note 8b).

4. INVENTORIES

	2010	2009
Completed goods	\$ 2,010,150	\$ 1,670,485
Works in progress	873	96,935
Raw materials	987,939	1,028,887
	\$ 2,998,962	\$ 2,796,307

5. PROPERTY, PLANT & EQUIPMENT

	2010 Cost	Accumulated Depreciation	2010 Net
Buildings	\$ 4,206,105	\$ 1,430,072	\$ 2,776,033
Building Improvements	1,044,367	—	1,044,367
Computer hardware	85,660	66,102	19,558
Furniture and fixtures	26,822	16,639	10,183
Office equipment	22,733	17,776	4,957
Manufacturing equipment	4,641,855	1,653,508	2,988,347
Trailer	27,479	13,544	13,935
Technology	134,480	—	134,480
Trade show booth	8,554	7,424	1,130
Truck	11,705	5,263	6,442
Land	472,795	—	472,795
	\$ 10,682,555	\$ 3,210,328	\$ 7,472,227

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	2009	Accumulated	2009
	Cost	Depreciation	Net
Buildings	\$ 4,171,305	\$ 1,385,381	\$ 2,785,924
Building Improvements	1,003,156	—	1,003,156
Computer hardware	83,725	63,022	20,703
Furniture and fixtures	26,170	15,693	10,477
Office equipment	21,973	16,929	5,044
Manufacturing equipment	4,481,619	1,608,101	2,873,518
Trailer	26,560	12,000	14,560
Technology	129,985	—	129,985
Trade show booth	8,268	7,088	1,180
Truck	11,313	4,582	6,731
Land	463,648	—	463,648
	\$ 10,427,722	\$ 3,112,796	\$ 7,314,926

Amount of depreciation expense for 2010: \$83,806 (2009: \$100,083)

The following carrying amount of capital assets held by Flexible Solutions Ltd. serves as collateral for the AFSC loan. (See Note 8b):

Land	\$ 273,703
Building	1,037,740
Building improvements	1,044,367
Manufacturing equipment	2,415,637
Trailer	13,934
Truck	6,441
Trade show booth	1,130
Technology	134,480

6. PATENTS

In fiscal 2005, the Company started the patent process for additional WATER\$AVR® products. Patents associated with these costs were granted in 2006 and they have been amortized over their legal life of 17 years.

Of the patents costs listed below, \$77,932 are not subject to amortization as of March 31, 2010, as the patents are still in the process of being approved.

	2010	Accumulated	2010
	Cost	Amortization	Net
Patents	\$ 260,975	\$ 31,734	\$ 229,241

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	2009	Accumulated	2009
	Cost	Amortization	Net
Patents	\$ 252,273	\$ 27,768	\$ 224,505

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Increase in 2010 cost was mainly due to currency conversion. 2010 cost in Canadian dollars - \$265,102 (2009 - \$264, 519 in Canadian dollars).

Amount of depreciation for 2010 - \$2,932 (2009 - \$1,864)

Estimated depreciation expense over the next five years is as follows:

2010	\$ 11,726
2011	11,726
2012	11,726
2013	11,726
2014	11,726

7. LONG TERM DEPOSITS

The Company has reclassified certain security deposits to better reflect their long term nature. Long term deposits consist of damage deposits held by landlords and security deposits held by various vendors.

	2010	2009
Long term deposits	\$ 7,741	\$ 7,499

8. LONG TERM DEBT

(a) Flexible Solutions Ltd. has received a non-interest bearing loan from the Department of Agriculture and Agri-Food Canada ("AAFC"). Eligible for up to \$1,000,000 Canadian funds, the Company had borrowed \$910,801 in Canadian funds (\$896,592) as of March 31, 2010, on an unsecured basis. If the full amount is borrowed, the repayment schedule is as follows:

<u>Amount Due (in CDN funds)</u>	<u>Payment Due Date</u>
\$200,000	January 1, 2012
\$200,000	January 1, 2013
\$200,000	January 1, 2014
\$200,000	January 1, 2015
\$200,000	January 1, 2016

(b) Flexible Solutions Ltd. has also received a 5% simple interest loan from Agriculture Financial Services Corp. ("AFSC"). Eligible for up to \$2,000,000 Canadian funds, the Company had borrowed \$1,491,000 in Canadian funds (\$1,418,687 US) as of March 31, 2010. The Company is required to make interest payments until May 1, 2010 and then must pay down the principal in equal payments until May 1, 2014. The Company has pledged its building in Taber, Alberta, as well as equipment, inventory and accounts receivable (see Notes 3 and 5) as collateral, as well as signed a promissory note guaranteeing the amount of the loan.

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Continuity:

Balance at December 31, 2008	\$ 1,546,836
Add: proceeds from long term debt	462,155
Effect of exchange rate	276,323
Balance at December 31, 2009	\$ 2,885,314
Effect of exchange rate	79,019
Balance at March 31, 2010	\$ 2,364,333

Outstanding balance at:	2010	2009
a) Long term debt – AAFC	\$ 896,593	\$ 866,627
b) Long term debt – AFSC	1,467,740	1,418,687
Long term debt	\$ 2,364,333	\$ 2,285,314
Less current portion	(106,420)	(74,146)
	\$ 2,257,913	\$ 2,211,168

9. STOCK OPTIONS

The Company adopted a stock option plan (“Plan”). The purpose of this Plan is to provide additional incentives to key employees, officers, directors and consultants of the Company and its subsidiaries in order to help attract and retain the best available personnel for positions of responsibility and otherwise promoting the success of its business. It is intended that options issued under this Plan constitute non-qualified stock options. The general terms of awards under the option plan are that 100% of the options granted will vest the year following the grant. The maximum term of options granted is 5 years.

The Company may issue stock options and stock bonuses for shares of its common stock to provide incentives to directors, key employees and other persons who contribute to the success of the Company. The exercise price of all incentive options are issued for not less than fair market value at the date of grant.

The following table summarizes the Company’s stock option activity for the years ended December 31, 2008, 2009 and the period ended March 31, 2010:

	Number of shares	Exercise price per share	Weighted average exercise price
Balance, December 31, 2007	1,912,440	\$3.040 - \$4.60	\$3.38
Granted	203,000	\$3.60	\$3.60
Cancelled or expired	(204,740)	\$3.00 - \$4.60	\$3.74
Balance, December 31, 2008	1,910,700	\$3.00 - \$4.55	\$3.38
Granted	122,000	\$2.25	\$2.25
Cancelled or expired	(486,000)	\$3.00 - \$4.55	\$3.44
Balance, December 31, 2009	1,546,700	\$2.25 – 3.85	\$3.25
Granted	155,000	\$1.50 – 2.25	\$1.84
Balance, March 31, 2010	1,701,700	\$1.50 – 3.85	\$3.12

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The fair value of each option grant is calculated using the following weighted average assumptions:

	2010		2009	
Expected life – years	5.0		5.0	
Interest rate	1.4	%	1.14	%
Volatility	60	%	65	%
Dividend yield	—	%	—	%
Weighted average fair value of options granted	\$ 0.31		\$ 1.01	

During the three months ended March 31, 2010 the Company granted 61,000 options to consultants that resulted in \$5,008 in expenses this quarter. During the same period, 94,000 options were granted to employees, resulting in \$7,021 in expenses this quarter. Options granted in previous quarters resulted in additional expenses in the amount of \$5,285 for consultants and \$10,871 for employees during the quarter ended March 31, 2010. No stock options were exercised during the period.

During the three months ended March 31, 2009 the Company granted 61,000 options to consultants that resulted in \$15,346 in expenses during the quarter. During the same period, 61,000 options were granted to employees, resulting in \$15,347 in expenses during the quarter. No stock options were exercised during this period.

10. WARRANTS

On April 14, 2005, the Company announced that it had raised \$3,375,000 pursuant to a private placement. The investors in this offering purchased 900,000 shares of the Company's common stock at a per-share price of \$3.75, together with warrants to purchase up to 900,000 additional shares of the Company's common stock. The warrants originally had a 4 year term and were exercisable at a price of \$4.50 per share.

On June 8, 2005, the Company announced that it had raised an additional \$327,750 pursuant to a private placement. An investor purchased 87,400 shares of the Company's common stock at a per share price of \$3.75, together with a warrant to purchase up to 87,400 additional shares of the Company's common stock. The warrants originally had a 4 year term and were exercisable at a price of \$4.50 per share.

In February 2009, the Company amended the warrants granted in 2005 to a per share exercise price of \$4.00 and extended the exercise term until July 31, 2009.

In May 2007 the Company closed a \$3,042,455 private placement with institutional investors. The Company sold 936,140 units at a price of \$3.25 per unit. Each unit consisted of one share of common stock and one-half warrant with a three year term and an exercise price of \$4.50 per share. The Company also issued 21,970 warrants with the same terms for investment banking services related to this transaction.

In February 2010, the Company amended the warrants granted in 2007 to a per share exercise price of \$3.00 and extended the exercise term until December 31, 2010.

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The following table summarizes the Company's warrant activity for the three years ended December 31, 2009 (no subsequent activity):

	Number of shares	Exercise price per share	Weighted average exercise price
Balance, December 31, 2007 and 2008	1,477,440	\$ 4.50	\$ 4.50
Granted	—	—	—
Exercised	—	—	—
Cancelled/Expired	987,400	\$ 4.50	\$ 4.50
Balance, December 31, 2009	490,040	\$ 3.00	\$ 3.00

11. CAPITAL STOCK.

The Company did not issue any shares of its common stock during the three months ended March 31, 2010.

12. SEGMENTED, SIGNIFICANT CUSTOMER INFORMATION AND ECONOMIC DEPENDENCY.

The Company operates in two segments:

(a) Development and marketing of two lines of energy and water conservation products (as shown under the column heading "EWCP" below), which consists of a (i) liquid swimming pool blanket which saves energy and water by inhibiting evaporation from the pool surface, and (ii) food-safe powdered form of the active ingredient within the liquid blanket and which is designed to be used in still or slow moving drinking water sources.

(b) Manufacture of biodegradable polymers ("BCPA's") used by the petroleum, chemical, utility and mining industries to prevent corrosion and scaling in water piping. This product can also be used in detergents to increase biodegradability and in agriculture to increase crop yields by enhancing fertilizer uptake.

The accounting policies of the segments are the same as those described in Note 2, *Significant Accounting Policies*. The Company evaluates performance based on profit or loss from operations before income taxes, not including nonrecurring gains and losses and foreign exchange gains and losses.

The Company's reportable segments are strategic business units that offer different, but synergistic products and services. They are managed separately because each business requires different technology and marketing strategies.

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Three months ended March 31, 2010:

	EWCP	BPCA	Total
Revenue	\$ 280,800	\$ 3,104,046	\$ 3,384,846
Interest revenue	—	—	—
Interest expense	17,794	948	18,742
Depreciation and amortization	11,278	75,460	86,738
Segment profit (loss)	(413,520)	929,193	515,673
Segment assets	5,180,735	2,520,733	7,701,468
Expenditures for segment assets	75,876	444	76,320

Three months ended March 31, 2009:

	EWCP	BPCA	Total
Revenue	\$ 211,267	\$ 2,448,281	\$ 2,659,548
Interest revenue	—	—	—
Interest expense	10,173	1,212	11,385
Depreciation and amortization	13,065	87,018	100,083
Segment profit (loss)	(307,893)	174,663	(133,230)
Segment assets	3,351,638	2,830,683	6,182,321
Expenditures for segment assets	202,857	2,903	205,760

The sales generated in the United States and Canada are as follows:

	2010	2009
Canada	\$ 165,914	\$ 87,572
United States and abroad	3,218,932	2,601,976
Total	\$ 3,384,846	\$ 2,659,548

The Company's long-lived assets are located in Canada and the United States as follows:

	2010	2009
Canada	\$ 5,180,735	\$ 4,943,238
United States	2,520,733	2,596,193
Total	\$ 7,701,468	\$ 7,539,431

Three customers accounted for \$2,025,581 (59%) of sales made in the period (2009 - \$1,581,211 or 59%).

13. COMMITMENTS.

The Company is committed to minimum rental payments for property and premises aggregating approximately \$406,850 over the term of three leases, the last expiring on December 31, 2011.

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Commitments in each of the next five years are approximately as follows:

2010	\$ 120,364
2011	86,502
2012	74,983
2013	78,025
2014	46,976

14. CONTINGENCIES.

On May 1, 2003, the Company filed a lawsuit in the Supreme Court of British Columbia, Canada, against John Wells and Equity Trust, S.A. seeking the return of 100,000 shares of its common stock and the repayment of a \$25,000 loan which were provided to the defendants for investment banking services. The services were not performed and in the proceedings the Company sought the return of the shares and the repayment of the loan. On the date of issuance, the transaction was recorded as shares issued for services at a fair market value of \$0.80 per share. On April 30, 2009 the Supreme Court of British Columbia ruled in favor of the Company and ordered Equity Trust S.A. to return the 100,000 shares and repay the loan with interest (\$30,514US). The Company has reversed the expense recorded for the shares in the year ended December 31, 2009.

15. SUBSEQUENT EVENTS.

None.

16. COMPARATIVE FIGURES.

Certain of the comparative figures have been reclassified to conform with the current year's presentation.

Item 2. Management’s Discussion and Analysis of Results of Operation and Financial Condition.

Overview

The Company develops, manufactures and markets specialty chemicals that slow the evaporation of water. The Company also manufactures and markets biodegradable polymers which are used in the oil, gas and agriculture industries.

Results of Operations

The Company has two product lines:

Energy and Water Conservation products - The Company’s HEAT\$AVR® product is used in swimming pools and spas. The product forms a thin, transparent layer on the water’s surface. The transparent layer slows the evaporation of water, allowing the water to retain a higher temperature for a longer period of time and thereby reducing the energy required to maintain the desired temperature of the water. WATER\$AVR®, a modified version of HEAT\$AVR®, can be used in reservoirs, potable water storage tanks, livestock watering ponds, canals, and irrigation ditches.

BCPA products - The second product, TPA’s (i.e. thermal polyaspartate biopolymers), are biodegradable polymers used by the petroleum, chemical, utility and mining industries to prevent corrosion and scaling in water piping. This product can also be used in detergents to increase biodegradability and in agriculture to increase crop yields by enhancing fertilizer uptake.

Material changes in the Company’s Statement of Operations for the three months ended March 31, 2010 are discussed below:

Three Months Ended March 31, 2010

<u>Item</u>	<u>Increase (I) or Decrease (D)</u>	<u>Reason</u>
Sales		
EWCP products	I	Increase in customer inventory to more normal level has resulted in greater sales.
BPCA products	I	Return to more normalized business in 2010 as opposed to 2009 has resulted in greater revenue across the division.

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Gross Profit	I	Increased sales.
Wages	I	Increased sales.
Research	I	New product development.
Office and miscellaneous	I	Various administrative costs associated with the start up of the new facility have been allocated to this account. Once the facility is operational, these costs will be allocated to overhead.

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Rent	D	A lease at a former location expired in 2009.
Commissions	I	Increased sales for the quarter resulted in higher commissions.
Utilities	I	Increased work at the Taber plant has required increased used of energy. Once the facility is operational, these costs will be allocated to overhead.

Capital Resources and Liquidity

The sources and uses of funds are directly obtainable from the Consolidated Statement of Cash Flows included as part of the financial statements filed with this report.

The Company has sufficient cash resources to meets its future commitments and cash flow requirements for the coming year. As of March 31, 2010 working capital was \$6,175,947 (2009 - \$6,242,378) and the Company has no substantial commitments that require significant outlays of cash over the coming fiscal year.

The Company is committed to minimum rental payments for property and premises aggregating approximately \$406,850 over the term of three leases, the last expiring on December 31, 2011.

Commitments in each of the next five years are approximately as follows:

2010	\$ 120,364
2011	86,502
2012	74,983
2013	78,025
2014	46,976

See Note 2 to the financial statements included as part of this report for a description of the Company's significant accounting policies and recent accounting pronouncements.

Item 4T. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the direction and with the participation of our management, including our Principal Executive and Financial Officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2010. We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our periodic reports with the Securities and Exchange Commission is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and regulations, and that such information is accumulated and communicated to our management, including our principal executive and financial officer, as appropriate, to allow timely decisions regarding required disclosure. Our disclosure controls and procedures are designed to provide a reasonable level of assurance of reaching desired disclosure control objectives. Based on the evaluation, our Principal Executive and Financial Officer concluded that these disclosure controls and procedures are effective as of March 31, 2010.

Changes in Internal Control over Financial Reporting

Our management, with the participation of our Principal Executive and Financial Officer, evaluated whether any change in our internal control over financial reporting occurred during the three months ended March 31, 2010. Based on that evaluation, it was concluded that there has been no change in our internal control over financial reporting during the three months ended March 31, 2010 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II

Item 6. Exhibits.

NumberDescription

- 3.1 Amended and Restated Certificate of Incorporation of the registrant. (1)
- 3.2 Bylaws of the registrant. (1)
- 31.1 Certification of Principal Executive Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002.*
- 31.2 Certification of Principal Financial Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002.*
- 32.1 Certification of Principal Executive and Financial Officer Pursuant to 18 U.S.C. §1350 and §906 of the Sarbanes-Oxley Act of 2002.*

* Filed with this report.

(1) Incorporated by reference to the registrant's Registration Statement on Form 10-SB (SEC File. No. 000-29649) filed February 22, 2000.

SIGNATURES

In accordance with the requirements of Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

May 13, 2010

FLEXIBLE SOLUTIONS INTERNATIONAL, INC.

By: /s/ Daniel B. O'Brien
Name: Daniel B. O'Brien
Title: President and Principal Executive Officer

By: /s/ Daniel B. O'Brien
Name: Daniel B. O'Brien
Title: Principal Financial and Accounting Officer